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### Contractual and Other Considerations Affecting Producers, Pipelines and Distributors During Current Period of Market Demand Constraints [outline]

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NATURAL GAS SYMPOSIUM: CONTRACT  
SOLUTIONS FOR THE FUTURE  
REGULATORY ENVIRONMENT

Sponsored By  
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Outline of Presentation  
By  
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Washington, DC

CONTRACTUAL AND OTHER CONSIDERATIONS  
AFFECTING PRODUCERS, PIPELINES AND  
DISTRIBUTORS DURING CURRENT PERIOD  
OF MARKET DEMAND CONSTRAINTS

I. CONTRACTUAL AND OTHER CONSIDERATIONS AFFECTING  
PRODUCERS, PIPELINES AND DISTRIBUTORS DURING  
CURRENT PERIOD OF MARKET DEMAND CONSTRAINTS

I. CURRENT MARKET CONDITIONS

A. Characteristics

1. High Prices.
2. Abundant Supply.
3. Declining Demand.

B. Causes

1. Natural Gas Policy Act of 1978.
  - a) Established higher ceiling prices for all categories of gas.
  - b) Provided that prices would escalate with inflation.
  - c) Provided "real growth" escalation for certain categories of gas.
  - d) Provided for deregulation of certain high cost gas.
2. Traditional Gas Purchasing Relationships and Patterns.
3. Indefinite Escalator Clauses.
4. Declining Alternative Fuel Prices.
5. Recession.
6. Conservation.
7. Warm Winter.

II. NEGOTIATING NEW CONTRACTS AND MODIFYING EXISTING  
SUPPLIER/PURCHASER RELATIONSHIPS IN RESPONSE  
TO MARKET CONDITIONS

A. Pipeline Concerns:

1. Negotiation of contracts with producers:
  - a) Reduction or elimination of take-or-pay obligations.
  - b) Market-out clauses in contracts for deregulated and other high cost gas.
  - c) Restructure pricing provisions.
  - d) Provisions permitting redetermination of contract price down to market-clearing level.
2. Filing new tariffs to modify existing rates to customers.
  - a) Discount/incentive rates to distributors and large industrial customers in order to minimize load loss to alternative fuels.

B. Producer Concerns:

1. Adequate consideration from purchasers in negotiating pricing clauses, take-or-pay and make-up clauses, market-out clauses, production related (i.e. gathering, compression, etc.) clauses and related provisions in existing and new contracts.
2. Sales levels to assure cash flow continuity.
3. Alternative transportation relationships.

C. Distributor Concerns:

1. Ability to renegotiate existing relationships with suppliers.

2. Options which can be used to influence pipeline suppliers and provide protection from marketability problems.
  - a) Alternative rate design proposals for pipeline suppliers.
  - b) Challenges to suppliers' PGA pass-throughs of high gas costs.
  - c) Challenges to supplier's minimum bill provisions in rate cases.
3. Two-part rate structures at the local level, charging industrial customers on a different basis than other customers in order to minimize industrial load loss.
4. Purchasing gas at the wellhead and establishing transportation arrangements for system supply.

### III. NON-CONTRACTUAL RESPONSES TO MARKETABILITY PROBLEMS

#### A. Producers

1. NGPA §311(a) arrangements to bypass traditional pipeline customers.
2. Direct sales to end users or distributors.
3. Constructing pipelines from supply area and recoupment of costs.
  - a) NGPA consequences.
  - b) Natural Gas Act consequences.

#### B. Pipelines ,

1. Off-System sales to market surplus gas supplies.
2. Incentive pricing policies to attract new loads.

C. Distributors

1. Alternative supply options.

- a) From other accessible pipeline suppliers.
- b) From producer field supply sources.
- c) Transportation arrangements under NGPA §311(a).
- d) The Illinois Commerce Commission has recently ordered three Illinois distributors to report on methods of obtaining alternative sources of gas supply.

D. Regulatory and Legislative Responses To Current Market Conditions

1. FERC.

- a) Regulatory scrutiny of traditional contractual provisions e.g. take-or-pay (see FERC Docket No. PL83-1-000), minimum bills, indefinite escalators, redeterminations.
- b) Check on pipeline purchasing practices under NGPA §601(c) "Fraud and Abuse" standard (PL82-1-000).
  - i) Columbia Gas Transmission Co. initial decision (TA81-1-21-001 and TA81-2-21-001).
  - ii) Petition of Associated Gas Distributors for a declaratory order that "abuse" encompasses certain pipeline gas purchasing practices (RM83-55-000).
- c) "Net-back" pricing approach to link wellhead price with price of alternative fuels at the burner tip.
- d) Pipeline rate designs giving pipelines incentive to avoid load loss due to high gas costs, i.e. a sliding scale rate of return based on sales volumes.

- e) Discount rates to industrial users in pipeline tariffs.
- f) Cap on §107 high cost gas at the commodity value of gas or some other level (RM82-32-000).

2. Potential Congressional Responses:

- a) Natural gas pipelines as common carriers.
- b) Decontrol wellhead prices (See Richard Morgan's presentation).
- c) Freeze or extend controls on wellhead prices.
- d) Impose market-out provisions legislatively.
- e) Abrogate or modify take-or-pay and indefinite pricing provisions in existing contracts.
- f) Abrogate contracts to permit renegotiation for a specified period.
- g) Direct FERC to exercise stricter scrutiny of pipeline pass-throughs under NGPA §601(c).
- h) Limit FERC discretion to administratively increase ceiling prices under the NGPA.
- i) Limit prices for imported natural gas.